How Unique Was The Chicago Tradition? - Introduction

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Chapter 23: How Unique was the Chicago Tradition?

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The first part of this chapter describes and elaborates upon the contributions made to this expanding literature by Tom Cate, J. Ronnie Davis, David Laidler, Joseph Aschheim and George Tavlas regarding the claim that inter-war Chicago exhibited unique quantity theory characteristics. The second part examines the so-called “Chicago Plan’ of Banking Reform”, described by Albert Hart (1935), a Chicago graduate student of the 1930s. The Chicago Plan was a response to the Great Depression which required all banks to hold 100% reserves against their deposits, thus eliminating the instability caused by fractional reserves.

23.1 Tavlas versus Cate, Davis and Laidler
There are parallels between the somewhat heated exchanges between Tavlas and his critics and Don Patinkin’s response to Michael Parkin. Also, there are similarities between aspects of Milton Friedman’s limited response to Patinkin and Arthur Pigou’s limited response to John Maynard Keynes. An analysis of these exchanges may also provide some wider insights into the nature of disputation in economics.

In the General Theory, Keynes (1936) assaulted the Marshallian tradition generally, and Pigou in particular. Pigou’s loyalty lay with the social reforming ideology of the Marshallian School. On several occasions, Pigou (1936; 1945; 1946; 1950) reflected on the General Theory. He defended Alfred Marshall from Keynes’ attacks but was less concerned for his own reputation. Pigou (1935, 22-4; 1931, 544) objected to Keynes’ “Body-line bowling!” and regarded “controversy for its own sake” as “a prodigious waste of time”. Moreover, “Controversies conducted in the manner of Kilkenny cats” undermined what he regarded as the potentially beneficial influence of economists. In consequence, Pigou became an involuntary accomplice in the cultivation of the ahistorical Keynes-Classics mythology.

Friedman (chapter 2 [1956]) launched the monetarist counter-revolution by minimising the originality of his own contribution and maximising the supposed contribution of the Chicago Fathers. When criticised privately by Patinkin, Friedman (chapter 4 [1968]) deleted the references to Chicago in his encyclopaedia article on the quantity theory. When criticised publicly by Patinkin, Friedman (chapter 7 [1972/1974], 167) responded: “After all, I am not unwilling to accept some credit for the theoretical analysis in that article”. Patinkin devoted a considerable amount of time and energy to examining his 1944 Economics 330 notes. According to Stanley Fischer (to Patinkin 16 March 1971), Friedman grumbled that he did not have “the time to be involved in polemics”. He either recalled, or examined his Archives, to provide David Laidler (1999, 239, n32) with information about Hawtrey’s Currency and Credit being on Lloyd Mints’ 330 reading list. But he did not examine his 1932 Economics 330 notes: “It was indeed stupid of me in the early 70’s not to go back to my notes, and as of this date I cannot really say why I did not think of doing so” (correspondence to the author, 29 November 2000). He thus directly contributed little
to the debate (beyond the initial irritation to Patinkin, and the subsequent retraction of his assertion about Chicago uniqueness and immunity to the Keynesian virus).

For twenty-five years, Tavlas has been adding to the literature while providing stimulating irritation to those who believed that the evidence favoured Patinkin. He traced the money growth rule back to Jeremy Bentham, Henry Thornton and John Gray (1977) and contributed some “notes” on Carl Snyder (1982). As a graduate student at New York University, Tavlas added “some further observations” to the debate and analysed the work of Senator Paul Douglas, an important Chicago economist of the 1930s and 1940s (chapter 24 [1976]; chapter 30 [1977]).

In conjunction with Aschheim, Tavlas explored the relationship between Monetarism and Ideology (chapter 32 [1979], 172). Whereas the laissez faire wing of the first generation Chicago School advocated discretionary changes in the money supply, Douglas, from the socialist-planning wing of the Chicago School, advocated a policy norm “strikingly reminiscent of the monetary growth-rule advocated by contemporary monetarists”.

In his first contribution, Tavlas (chapter 24 [1976], 692, 685-6) argued that “to [William] Foster and [Waddill] Catchings, and the Chicagoans, public works were a means of conducting monetary policy”. Keynes and his followers advocated budget deficits “within a theoretical framework that featured the impotence of monetary policy during depressions”. In contrast, “American economists – especially members of the Chicago School – advocated budget deficits precisely because monetary policy did matter” [emphasis in original].

Within the Keynesian framework, $Y = C + I + G$ (where $Y$ = national income, $C$ = consumption, $I$ = investment, and $G$ = government expenditure), there is a direct theoretical route whereby an increase in $G$ can increase $Y$. Tavlas also demonstrated that within the Chicagoan quantity theory framework, $MV = PT$ (where $M$ = the quantity of money, $V$ = the velocity of money, $P$ = the price level, and $T$ = the level of output), an identical result could be achieved, with fiscal deficits increasing $M$. Hence, he argued, the immunity of Chicagoans from the influence of the General Theory.

This framework was also an important ingredient of Patinkin’s (chapter 5 [1981/1969], 245-6) “Other Chicago” (as distinct from “Friedman’s Chicago” which Patinkin sought to debunk). The “Other Chicago” was, according to Patinkin, ‘primarily a summary of Simons’ views, which were largely accepted by Mints” and to a lesser extent by Frank Knight and Jacob Viner. In what Patinkin regarded as this authentic Chicago tradition, “the government had an obligation to undertake a contracyclical policy. The guiding principle of this policy is to change $M$ so as to offset changes in $V$, and thus generate the full-employment level of aggregate demand $MV$ … The necessary variations in $M$ can be generated either by open-market operations or by budgetary deficits. The latter method is more efficient, and in some cases might even be necessary. Budgetary deficits, in turn, can be generated by varying either government expenditure or tax receipts. From the point of view of contracyclical policy, this makes no difference – for either method changes $M$”. Patinkin contrasted “his” Chicago with Friedman’s, but not with other contemporaneous approaches to the business cycle.
Tavlas (chapter 35 [1998], 219-220) argued that Patinkin and Harry Johnson “overlooked that lonely spot on the Midway that used the quantity theory to provide an alternative rationale for a policy of public works during the Depression”. Tavlas also argued that Friedman was “expounding the old time-religion which insisted that money mattered”. Thus “while some economists outside Chicago advocated the use of expansionary fiscal measures, only the Chicagoans used the quantity theory to rationalise such a policy. Only the Chicagoans identified the use of fiscal measures as a direct mechanism to effectuate an increase in the money supply”. This 1930s Chicago “consensus” that “fiscal measures are a way of conducting monetary policy” was, according to Tavlas, “remarkable … I am not aware of a single US economist during the early 1930s outside the University of Chicago who explicitly and consistently used the quantity theory framework in such a manner”. Thus Tavlas identified a “uniqueness” which is different from that initially identified by Friedman.

Aspects of Tavlas’ work have been described as “excellent” (Cate chapter 28 [1981], 1132). But Davis (chapter 26 [1979], 921) suggested that Tavlas appeared to be writing in ignorance of the literature he was criticising, and Laidler (chapter 36 [1998]) suggested that he was writing in ignorance of the secondary literature. The conventional view is that underconsumptionists have typically confined their analysis to the real sector of the economy, and have thus, typically, downplayed the importance of monetary factors (see, for example, Schneider 1987, 742). Conventional views are legitimate targets for scholars, although they have to be subjected to detailed criticism for any radical reinterpretation to have any chance of widespread acceptance. Laidler (1999, 211, n28; Laidler chapter 36 [1998], n1) argued that Foster and Catchings, Douglas and John Gray were underconsumptionists and that Tavlas’ attempts to portray them as quantity theorists “seems quite indefensible in light of the textual evidence”. It was therefore “utterly unhelpful” for Tavlas to “gloss over” the division between underconsumptionism and the quantity theory: “Perhaps other historians of economic thought will agree with me”.

Tavlas has, so far, engaged three opponents. The first, Davis (chapter 25 [1968]) provided a path breaking analysis of the Chicago economists of the 1930s, followed by an extensive analysis of The New Economics and the Old Economists (1971). Tavlas (chapter 24 [1976], 688) argued that Davis had blurred the “very sharp differences between the U.S. economists, especially the residents at Chicago, and Keynes”. Moreover the work of Foster and Catchings had not been adequately appraised in this context.

In response, Davis (chapter 26 [1979], 919, 921) concluded that Tavlas’ “corrective … is itself adulterated”; Tavlas had committed “a serious error” by “misreading” his book. Davis titled his reply “The Last Remake of the The New Economics and the Old Economists” but added that “the character of the controversy” was unlikely to allow an immediate termination. Tavlas, in turn, suggested that Davis had “failed to identify the Chicagoans of the 1930s as quantity theorists”. The monetary economics of Foster and Catching and the Chicagoans “helped identify the historical foundations of the monetarist counter-revolution, including the reasons underlying the Chicago School’s resistance to the Keynesian virus”.
Tom Cate (chapter 28 [1981], 1132-3, 1135-6) located what he believed to be “a serious error” in Tavlas’ argument which was based on an “inaccurate reading of the Treatise and the General Theory”. According to Cate, the policy recommendations of the Treatise (which Keynes repeated in Chicago in 1931) were “identical to the policies which he advocates in his earlier writings”. Thus the transformation in Keynes’ analysis towards a loan-financed domestic investment program occurred after Keynes’ visit to Chicago.

In response, Tavlas (chapter 29 [1981], 1139) argued that Keynes’ “theoretical thinking had undergone a marked change” by the time of the publication of the Treatise. Thus by emphasizing the continuity in Keynes’ work between 1923 and 1931, Cate “obscures the transformation of Keynes’ own thinking on monetary economics and obviates one of the reasons why, in the initial stages, the monetarist counter-revolution was centred in Chicago. In particular, in the Tract Keynes expounded views on monetary theory similar to those which were later to categorize the 1930s Chicago School. Keynes’ rejection of these views in the Treatise explains, in part, the Chicago School’s resistance to the Keynesian revolution”.

According to Tavlas (chapter 29 [1981], 1140), Pigou and Keynes of the Tract analysed the quantity theory using a choice theoretic demand for money approach, thus displaying a “basic similarity with the macroeconomics of the Chicago school of the 1930s”. But in the Treatise, this approach had been replaced by “the controversial and short-lived fundamental equations”. After his visit to Chicago in 1931, Keynes “began to share the Chicago view that banking measures were insufficient in dealing with the 1930s depression. Moreover – and in accord with the Chicagoans – Keynes increasingly opted for budget deficits to combat the depression. Where he departs from the Chicagoans, however, is in his rejection regarding the compatibility of budget deficits within the framework of the quantity theory. Instead, Keynes elected to construct a new theoretical structure to support his practical recommendations of public works projects”.

Tavlas’ next adversary was Laidler, the author of The Golden Age of the Quantity Theory: the Development of Neoclassical Monetary Economics 1870-1914 (1991); Fabricating the Keynesian Revolution: Studies of the Inter-War Literature on Money, the Cycle, and Unemployment (1999); and The Demand for Money: Theory and Evidence (1969) which in its third edition became The Demand for Money: Theory, Evidence and Problems (1985). Laidler’s interest in the Chicago tradition presumably extends back to his experience of having been taught by Friedman at Chicago in the early 1960s. Laidler became a monetarist, albeit one critical of Friedman’s formulation of the demand for money function (Laidler 1966).

Tavlas (chapter 30 [1977]) argued that while Douglas is primarily remembered, at an academic level, for the Cobb-Douglas production function, he also utilised a monetary framework. Douglas was “above all” a quantity theorist. Tavlas concluded that Friedman was correct in delineating a unique Chicago quantity theory tradition. Moreover, Douglas’ pre-1936 contribution “was a major reason why Chicago became immune from the Keynesian virus”. Tavlas (chapter 31 [1981]) explored the evolution of two traditions: a cost-push explanation of inflation culminating in the Radcliffe Report and a Chicago quantity theory tradition culminating in monetarism.
Friedman was the “beneficiary” of this Chicago tradition; whereas the Keynesians had “misconstrued” their “master’s message”.

In contrast, Laidler (chapter 33 [1993]) argued that some of the distinctive characteristics that Friedman attributed to Chicago in the 1930s were present in the work of two Harvard economists, Allyn Young and his student, Lauchlin Currie, and in the writings of the British Treasury economist, Ralph Hawtrey. Before his retirement, Hawtrey had only one academic appointment – at Harvard as Young’s replacement (1928-9), with Currie as his assistant. Judged by the citation count, Hawtrey and Young exerted an almost equivalent influence upon the first version of Currie’s thesis. Young also taught James Angell, Edward Chamberlin, Frank Knight, Harold Reed and Arthur Marget and so exerted a considerable influence over interwar monetary economists (Blitch 1995, 115; Laidler 1999, 197, n14, 234, n24; Moggridge 1992, 882; Bigg 1987, 605).

Using Friedman’s (1953) widely imitated methodological distinction, Laidler (chapter 33 [1993]) found the “positive” theoretical content of the Chicago tradition to be essentially indistinguishable from this Harvard-Hawtrey tradition; whereas the “distinctive feature of Chicagoan analysis was normative, namely to forge a link between a monetary explanation of the cycle and a liberal political agenda”. Laidler provided support for Patinkin’s conclusion: in inter-war Chicago in the 1930s and 1940s the quantity theory was not “first and foremost” a theory of the demand for money.

Scholars are understandably irked when their hard-earned publications are not cited, even when no snub was intended. According to Tavlas (correspondence to the author 9 May 2002), Laidler had committed “pre-selection sample bias” by failing to cite his work. Tavlas (chapter 40 [1999], 242) complained that “Laidler does not even refer to [Tavlas chapter 30, 1997] – but deflects attention away from it by diverting the reader to references that are not aimed at addressing the particular issues”. Knight (1935, 355), the pre-eminent first generation Chicago sociologist of economic knowledge noted that “we must recognise that there is in our field no objective test for separating either truth from opinion or the urge to promote an opinion ‘believed’ to be true from the craving for personal aggrandisement”. George Stigler, the pre-eminent second generation Chicago sociologist of economic knowledge, noted that “Even to be demolished is better for one’s self-esteem than to be ignored”. Tavlas, believing that his evidence had not been adequately treated, presented an uncompromising critique of Laidler’s interpretation.

Laidler and Roger Sandilands (chapter 41 [2002]) provide an introductory note to a 1932 Harvard Memorandum on anti-depression policy authored by Currie, Paul Theodore Ellsworth and Harry Dexter White (chapter 42 [1932]). They conclude that “there was nothing unique about the Chicago tradition as it stood in early 1932”. Friedman acknowledged in correspondence to Laidler (chapter 41 [2002]) that he has withdrawn his assertion about uniqueness: the Memorandum “certainly supports your position that Chicago had no monopoly on the quantity theory approach to the Great Depression and to measures required to recover from it”.

With respect to the immunity argument, Tavlas provided evidence supporting Friedman’s (chapter 7 [1972/1974], 162) initial position about “remaining largely
unaffected and if anything somewhat hostile [to] … the Keynesian revolution”. However, in his Memoirs, Friedman reversed his judgement about his own personal immunity from Keynesianism. He was “shocked” to re-read his wartime essays with their unmistakably Keynesian taint. During the war, Friedman drafted speeches for the Secretary of the Treasury and made statements before congressional committees. In a statement in 1942 before the House Ways and Means Committee, Friedman declared that “inflation … must be neutralised by measures that restrict consumer spending. Taxation is the most important of those measures”. Looking back he was shocked: “The most striking feature of this statement is how thoroughly Keynesian it is. I did not even mention ‘money’ or ‘monetary policy’! The only ‘methods of avoiding inflation’ I mentioned in addition to taxation were ‘price control and rationing, control of consumers’ credit, reduction in government and war bond campaigns’. Until I reread my statement to Congress in preparing this account, I had completely forgotten how thoroughly Keynesian I was then. I was apparently cured, some would say corrupted shortly after the end of the war” (Friedman and Friedman 1998, 115, 123, 112).

23.2 The Chicago Plan of Banking Reform

Tavlas (chapter 37 [1998], 20; chapter 35 [1998], 215) cited the “Chicago Plan of Banking reform” in support of his argument: “At a minimum, the Chicago faculty seemed to believe that these elements added up to a cohesive and unique oral tradition”. One of the elements of this “unique oral tradition” was “support for 100 per cent reserve requirements for banks … that was known as ‘The ‘Chicago Plan’ of Banking Reform” (Hart 1934-5)”.

However, it is not clear that the Chicago Plan provides any compensating support for the uniqueness argument. The preamble to the Plan explained that its purpose was to contribute towards the construction of a consensus of academic opinion: “it seems desirable that there should be some statement of opinion by academic economists, especially by groups [emphasis added] whose members hold substantially similar views” (cited by Phillips 1995, 192; see also Simons 1948 [1934], 76-7). Joseph Reeve (1943, 317, 191) in his history of the Monetary Reform Movements explained that the 100% money proposals appeared to have been “largely independent reactions to the cataclysm”. In her study of The Banking Crisis of 1933, Susan Kennedy (1973, 166-7) noted that “a host of academics bombarded” Roosevelt with reform proposals. These included proposals from John Dewey and the University of Minnesota, the University of Kansas and the University of Georgia. The Chicago plan was “typical of the recommendations offered at this time … Many of the proposals reiterated ideas submitted during the Glass bill debates”. Kennedy concluded that by the end of the 1930s a “substantial minority of leading economists” had rallied behind the proposal. Irving Fisher (1934a, 157) credited Robert Hempell of the Federal Reserve Bank of Atlanta, not the Chicago economists, as the initial American advocate of the proposal. Fisher (1935, ix) also listed 27 non-Chicago economists who supported 100% Money.

Albert Hart (1935, 104) described the Chicago Plan as coming from “several quarters … Simultaneously, and quite independently, the same notions were developed by Dr Laughlin [sic] Currie, of Harvard University.” In the footnote attached to that sentence, Hart referenced Currie’s Supply and Control of Money in the United States. Hart had been one of Currie’s students (Sandilands 1990, 25) and had alerted Currie
(1934, 156, n) to the Chicago Plan as his book was in press. Indeed, the Chicago Plan outlined by Hart (1935, 104) was not actually derived from Chicago at all. In the opening paragraph Hart explained that “Another independent inventor of very similar ideas was Mr Bostrom, now of the University of Texas whose proposals are sketched below. From conversations with various Americans I am convinced that the same notion occurred to economists at several other centres of economics at the same time, although their findings have not happened to be published”. One dissenting voice from the “standard form of the ‘100% per cent scheme’” came in the form of a Chicago oral tradition. Hart (1935, 106, n1) explained that the dissenting voice “which originates with Professor Frank Knight, has not – so far as I know – been advanced in any published writings”.

Henry Simons (1952 [1936], 356, n, 340-1, 358, n) minimised the significance of the 100% reserve proposal: “Standing by itself, as an isolated measure, it would promise little but evasion - small effects at the price of serious disturbance – and would deserve classification as merely another crank scheme”. Simons explained that the ‘Chicago’ reserve proposal was advanced together with the “eventual fixing of the total quantity of circulating media”. This, Simons suggested, was initially found “attractive” because it could “provide the basis of a new ‘religion of money’ around which might be regimented strong sentiments against tinkering with the currency”. But Simons emphasised that “this rule cannot now be recommended as a basis for monetary reform. The obvious weakness of fixed quantity, as a sole rule for monetary policy, lies in the danger of sharp changes on the velocity side”. Moreover, Simons indicated that the proposal was not unique to Chicago: “The so called 100 per cent scheme was suggested, at least by its Chicago proponents …”.

In his discussion of 100% money, Richard Lester (1939, 291-2) in his study of Monetary Experiments, directed readers to Fisher (1935), Currie (1934, chapter XV), Hart (1935), Angell (1935), and Frank Graham (1936). The advocates of the Chicago Plan were seen as part of a wider constituency which included Currie, Angell and Fisher (Goldenweiser 1951, 53). Angell noted that the 100% reserve idea was “not new either as theory or practice” (1935, 5; see also Lester 1935, 34). Harold Reed (1942, 436-7) noted that Simons and Currie had independently espoused the Plan but that “Angell’s ingenuity in modifying the details of the plan has increased interest by lessening the force of some of the practical objections”. Fisher (1934-5, 410) also discussed Angell’s implementation proposal in a favourable light. Leonard Watkins (1938, 22, 26-7) noted that Angell (unlike Frederick Soddy, Fisher or Simons) explicitly integrated his advocacy of the 100% proposal to his ultimate objective, in which he “virtually urges” the “stabilization of the total supply of money with an allowance for secular growth”.

Indeed, in his version of the 100% reserve Plan, Angell (1935, 17, n4, 27-8, n6) emphasised that his own development of the ‘monetarist’ component of the Plan predated and may have influenced the Chicago contribution. Angell criticised as “inadequate” the “Chicago group’s explanation of banking and business cycles, running chiefly in terms of ‘sticky’ prices”. Instead, he found “much more attractive” the idea of “keeping the quantity of money fairly stable over time, as there proposed (constantly or slowly increasing)”. This he believed “would impose a quite different and probably much stabler pattern of behavior on the economy than any we have hitherto experienced”. Referring to Angell (1933a, 1933b), he continued: “This
proposal is nearly the same as some suggestions I made in an address at the end of 1932”.

Watkins (1938, 16-7), Graham (1936, 428, n2) and Reed (1942, 436-7) all noted that the 100% proposal had been “first revived in recent years” by Soddy, the 1921 Nobel Laureate in Chemistry. Soddy (1943, 11) regarded Fisher’s 100% money plan as “practically identical” to his own and when banking reform was discussed in a broader context Soddy’s proposal was regarded as having been “popularized” by the advocates of the Chicago Plan (Watkins 1938, 20).

An asymmetrical ‘hysteresis’ explanation underpinned part of Soddy’s (1933a, 175) objection to the quantity theory which “works beautifully one way [emphasis in original]”. Increasing the quantity of money would in the short run increase wealth but in the long run increase prices alone. Reducing the quantity of money would permanently reduce “virtual wealth”. Thus Soddy (1934, 100) explained that “It is not necessary to consider this old ‘quantity theory’ of money farther than this, because enough has been said to show that it really is a fraud”. xxii

The hunt for precursors to Soddy began in the AER (Bromberg 1939, 553). Knight (1927, 732) was critical of the “cocky airs of the novice” that Soddy displayed. Simons (1935, 1421) described Soddy as a “presumptuous charlatan” but failed to mention the connection between Soddy’s 100% money proposal and the Chicago Plan. Alvin Hansen (1938, 111-3) – with whom Simons was feuding - sarcastically noted that it was “strange” that the Chicago Plan had not explicitly been connected to Soddy’s proposal. Hansen believed that the novelty of Simons’ exposition of Soddy’s proposal was its appropriation as part of the libertarian agenda. Simons (1939, 273, n1) took exception to being “chided” by Hansen who was guilty of a worse crime by allowing his discussion of precursors to come to a “stop with mention of Soddy!” Simons was also outraged by Hansen’s association of the “Chicago group” with Angell’s monetarism: “He classes us, along with Angell, as proponents of the fixed-quantity scheme and, by way of documentation, cites an article of mine … which is a complete disavowal of that scheme and an exposition of its crucial shortcomings. I cannot believe that Hansen has read this article with even ordinary care, for on other points as well his representation is distressingly unfaithful”. Hansen had “grossly misrepresented the views of [himself] and the so-called Chicago group on monetary policy”.

The process by which the monetary Chicago Plan proceeded through the political marketplace casts further light on the uniqueness case. It also illustrates the lack of one-to-one correspondence between monetarism and ideology highlighted by Aschheim and Tavlas (chapter 32 [1981]). Watkins (1938, 30, n11) noted that “Agitation for the plan has brought together ‘strange bedfellows’”. Indeed, the Chicago Plan may have acquired its name as a specific attempt to appeal to both Rexford Tugwell and Frederic A. Delano, President Roosevelt’s uncle and the chairman of the New Deal National Planning Board (1933-43), which became a vehicle for Alvin Hansen’s version of Keynesianism (Brinkley 2000, 175), xxiv In correspondence with Wesley Clare Mitchell, ex-President Hoover described the purpose of such a Board as the creation of “a Socialist State – or at least a Regimented one” (cited by Karl 1974, 244).
Delano had been interested in monetary reform since the 1896 US presidential election and after the panic of 1907, had founded a League to promote reform of the banking system. From the outset until 1918, he served on the Federal Reserve Board; between 1929-1933 he was President of the Stable Money Association (Reagan 1982, 47-8, 59). In the 1880s, he entered the railroad industry in Chicago during its period of maximum expansion. He became closely involved in what was known as the “Chicago Plan” of City Beautification and urban development.

Chicago was infamous throughout the world for its housing problems. Berliners had hoped that their city would become “Athens on the Spree”, but with the decline in the quality of their housing stock their city became known as “Chicago on the Spree”. The *JPE* published Delano’s (1913, 831) essay on ‘The Chicago Plan, with Particular Reference to the Railway Terminal Problem’ in which the Chicago Plan was presented as the coordinated “blow” which would strike at the heart of Chicago’s urban housing and congestion problems. The Chicago Plan became the prototype of other ‘Progressive’ Plans including the Regional Plan of New York, unveiled in 1929 (Reagan 1982, 55).

The original Chicago Plan envisaged a city larger than any other in the world (“an American Paris”), exerting primacy over a mid-continent domain larger than most European countries (Scott 1969, 107). In 1933, at the start of Chicago second World’s Fair, the Chicago Plan Commission published *The Chicago Plan in 1933 – Twenty-Five Years of Accomplishments* (Wrigley 1983, 70). In 1933 Roosevelt appointed Tugwell as Director of the Resettlement Administration. He was regarded as “America’s greenbelt advocate” with strong intellectual affinities with the Garden City ideals” which “included a belief in planning as a device to implement a broader social and economic restructuring of society” (Sies and Silver 1996, 5; Schuman and Sclar 1996, 437). In September 1932, Paul Douglas (one of the co-signatories of the Chicago Plan of Banking Reform) advocated planning as a vehicle to facilitate the provision of “great areas of forests and parks on the outside of every one of our cities [and] more decent housing within our cities” (cited by Aschheim and Tavlas chapter 32 [1979], 176-7).

On 16 March 1933, Knight sent what became known as the Chicago Plan of Banking Reform to Henry A. Wallace, Roosevelt’s first Secretary of Agriculture. In a follow-up memorandum to the President on 23 March 1933, Wallace described the “memorandum from the Chicago economists” as “really awfully good” and “a complete break with our present banking history” (cited by Phillips 1995, 198). The administrative debate over the Chicago Plan became centred on Wallace’s Department of Agriculture, where it was strongly supported by Gardiner Means and Tugwell. By 1934, the Chicago Plan had virtually become the Wallace-Tugwell-Means Plan; propagated by “numerous memos” from Means (Phillips 1995, 69-75).

The Department of Agriculture and the Wallace family were at the centre of many interwar controversies over proposals for economic reform. Agriculture Secretary Henry C. Wallace Sr. (Wallace’s father) supported the 1924 McNary-Haugen bill which proposed to fix the price of eight basic agricultural commodities (Hicks 1960, 198). In consequence, Hoover described Wallace Sr., his Cabinet colleague, as an “unwitting Fascist” (Barber 1985, 51, 208, n25). Hoover thus became known to the farming lobby as “the arch enemy of a fair deal for agriculture” (Hicks 1960, 201).
In 1922, Henry A. Wallace pushed President Harding to accept Thorstein Veblen, from the University of Chicago as an advisor to his Conference on Agriculture. Wallace hoped that business civilisation would be replaced by the rule of “production engineers” and “statistical economists”. He embraced John Dewey’s call for a “new individualism” based on farm cooperatives which could be expanded to include other sectors of the economy. Wallace was “contemptuous” of Hoover whom he regarded as “agriculture’s worst enemy” in the 1920s. After Hoover won the Republican nomination of 1928 he sought to mobilise support for a farm-orientated third party. When that push failed, he backed Hoover’s Democratic opponent (Markowitz 1973, 14, 18-9).

As Stigler (1962, 17) noted, Henry A. Wallace approved of institutionalised price fixing as a remedy for the farm problem. The agricultural plan of the brains trust (to restrict agricultural production) was in effect, a Chicago Plan, formulated by Wallace, Tugwell, and M.L. Wilson at two University of Chicago conferences on agriculture and planning in August 1931 and April 1932, just prior to Roosevelt’s nomination (Schapsmeier and Schapsmeier 1968, 149-52; Schlesinger 1957, 403; Kirkendall 1966, 31, 45). It was part of a wider belief that “a planned economy needed to be substituted for laissez faire in the light of the collapse of our business civilisation” (Elliot 1977, 193). Friedman (1962, 198) referred to the agricultural aspects of the New Deal reforms as “a national scandal that has wasted public funds”.

Hoover (1934, 100-1) described Roosevelt’s monetary initiatives as “the negation of whole philosophy of Liberty. Executive power over the coin is one of the oldest components of despotism”. Two decades after his electoral defeat, Hoover (1952, 408) was still denigrating the activities of the New Deal: “Along with currency manipulation, the New Deal introduced to Americans the spectacle of Fascist dictatorship to business, labor and agriculture”. Simons (1948 [1941], 91) provided similar abuse: “Any literate person may now identify Mr. [Henry A.] Wallace as our leading advocate of the totalitarian or pre-totalitarian economy of negotiation among tightly organised, monopolizing functional groups”. Wallace’s proposal to create post war international agricultural syndicates would create an American farming sector whose “power may be as inimical to peace as was that of Prussian landowners in the past” (Simons 1943, 442).

Tugwell was frequently accused of wishing to Sovietise America. In April 1934, Roosevelt nominated him as Undersecretary of Agriculture which led to him being grilled by the Senate about whether he was a communist (Sternscher 1964, 309, 9, 256). Among those employed in Henry A. Wallace’s Department of Agriculture were Alger Hiss and Adlai Stevenson (Schapsmeier and Schapsmeier 1968, 193, 203). James Paul Warburg noted in 1934 that of all the New Dealers, Tugwell and Wallace were the most sympathetic to the Soviet experiment (Markowitz 1973, 164). In 1946, despite pressure from the University President, the Chicago Economics Department “refused to appoint [Tugwell] to their faculty” (Friedman 1983, 188).

Henry A. Wallace believed that the New Deal needed to be run by a small group of economists: an economic Supreme Court or Council on the General Welfare (Zinn 1968, 68-76). His faith in planning led the American Liberty League to target him as a prime threat to capitalism. In response, he vigorously attacked the 1936 Republican
candidate, Alf Landon, as an agent of the Liberty League. After the demise of NRA, the Department of Agriculture became the focus of administrative attempts to institute economic planning and social reform (Markowitz 1973, 25-7).

Roosevelt insisted that Wallace be his Vice Presidential partner in the 1940 election. Had Roosevelt died a few months earlier, Vice President Wallace (1941-5) would have become President of the United States. As it was, he was removed from the platform, Truman succeeded Roosevelt and Wallace served as Truman’s Secretary of Commerce. In September 1946, Wallace made a speech to a pro-Soviet audience which was interpreted by some Europeans as evidence that the Americans were preparing to abandon them to the Russians. As a consequence, Truman sacked him (Manchester 1975, 319; Markowitz 1973, 28).

Eight days later a Conference of Progressives met in Chicago. With assistance from Tugwell, Paul Sweezy and Richard Watt (a University of Chicago Law professor), the 1948 Progressive party platform was organised with Wallace as the presidential candidate (Markowitz 1973, 201, 286, 173, 186-190). Wallace denounced the Marshall Plan as an anti-Soviet “Martial Plan” (Saunders 1966, 73). His party was perceived to be a communist front organisation: he planned to have Harry Dexter White as Treasury Secretary and the President of the United Electrical Workers Union as Secretary of Labor (Moley 1949, 85: Carr 1952, 337; Latham 1966, 396; Rees 1973, 408). William Buckley (1951, 87, 48, 231-2, 94-5) complained that Wallace’s supporters (armed with text books co-authored by Chicago trained economists) had captured Yale University for subversive purposes. In 1947-8, Buckley had been taught Economics 10 by Alexander Brooks who “energetically promoted Wallaces’s Communist-dominated Progressive Party in the spring of 1948”.xxii Albert Hart (1948, 471, n) complained that the “anti-Keynesian ’party line’” had mobilised a constituency which could successfully defeat any proposal linked to the names of Keynes or Henry Wallace.

In the mid-1930s, several Senators and Congressmen introduced Bills to facilitate the operation of the Chicago Plan (Watkins 1938, 23-4). One of these supporters was Californian Democrat Congressman, Jerry Voorhis (1938, 14), who combined it with the ‘monetarist’ suggestion that “We need to instruct our monetary authority – the Federal Reserve Board – to anticipate the nation’s need for an annual increase of circulating medium of about 4%”. For Voorhis (1947, chapter 13) this was “My Big Campaign”. Voorhis had been a member of the Yale University Liberal Club with Aaron Director in the early 1920s (Coase 1998). Voorhis (1947, 7-8, 15, 164) was a registered Socialist who voted for the Socialist Norman Thomas in 1928. When he discovered the works of Irving Fisher in the mid-1930s he wondered why he had not been exposed to these views whilst at Yale.

Voorhis was swept into Congress in the Democratic landslide of 1936 (Bullock 1978). He immediately enlisted Fisher into his own private “brain trust”. Voorhis sponsored a bill in Congress which Fisher interpreted as a method of implementing “central control of the circulating medium” (Fisher cited by Fisher 1956, 316). But the author of this Chicago Plan monetarism was defeated in the 1946 congressional election by Richard Nixon who declared the choice to be between “a supporter of free enterprise, individual initiative, and a sound progressive reform, or for my opponent who has supported by his votes the foreign ideologies of the New Deal Administration”.

According to Paul Douglas (1972, 237-8) Voorhis was “truly one of the saints of the earth”. According to Nixon, Voorhis was also associated in some way with “Wallace’s proposal that Russia be given a free hand” (Nixon cited by Voorhis 1973, 15).

Twenty-six years later (August 1972), this episode of history became a potent contemporary weapon for President Nixon in his determination to defeat George McGovern, his 1972 Democratic Party opponent. Douglas (1972, 237) recalled that in 1946, “anonymous character assassins” phoned electors to tell them that “Voorhis was a Communist … Jerry was defeated and Nixon was launched on a career that has now taken him to the White House”. Within the White House in 1972, it was calculated that McGovern could be portrayed as a subversive for his support of Wallace in the 1948 election (Safire 1975, 645). The following month the JPE published the exchange between Friedman and Patinkin (chapters 6 and 7 [1972/1974]) illustrating that for economists too, history can be a contemporary weapon.

In his essay on ‘The Literature of Economics’ Stigler (1978, 200-201) compared controversy in economics to “a series of simultaneous and intersecting fox hunts”. Economists tend to hunt in packs – driven in part by the thrill of the chase and perhaps even the scent of blood. Laidler (chapter 38 [1998]; Laidler 1999, 238, n30) titled his second response to Tavlas as “a final comment” – but since he also accused Tavlas of using “sarcasm” and being “patronizing” and “condescending” in presenting “irrelevant, and occasionally inaccurate” arguments, this particular foxhunt seems likely to continue.

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NOTES

i The Chicago Plan may have prompted the First National Bank of Englewood, located near the Chicago campus, to become 100% liquid in early 1934 (Phillips 1994, 18, n17).

ii Pigou continued: “It was, perhaps, a fault in Marshall that he discovered more truth in the writings of others than was actually there, and unduly depreciated his own contributions. There is no fault of that kind in Mr. Keynes!” Marshall’s generosity to his predecessors, was according to Pigou, “a great man’s fault, not a little man’s”.

iii Also, A.W.H. Phillips did not correct the errors that circulated about his work (Leeson 2002).

iv Don Patinkin Papers, Box 2.

v In his analysis of Monetary Reform Movements, Joseph Reeve (1943, 210, 219, xi-xii) identified a wide academic constituency in the 1930s in favour of monetary expansion through public works: “With the possible exception of the proposals for more aggressive open-market purchases and credit expansion by the Federal Reserve System during 1931-33, probably no major type of monetary expansion attracted more widespread public support from professional economists than did deficit spending, especially spending for public works construction”. Reeve reported that Harry Hopkins, the Works Progress Administrator, explained that the WPA dollar was “the fastest moving dollar in America”. Reeve’s book began as a Chicago PhD on ‘Monetary Proposals for Curing the Depression in the United States, 1929-1935’ with Mints as committee chairman (Patinkin chapter 5 [1981/1969], 262-3). Of the eight economists who either contributed “fundamental ideas” or who read and criticised Reeve’s manuscript before it “neared its final form”, five were Chicago economists (Mints, Viner, Lange, Simons and Knight), two were Chicago economists
at one remove (Charles Hardy and Homer Jones) and the eighth was at the Cowles Commission, which was on the Chicago campus (Dickson Leavens). A ninth, Paul Douglas, “first encouraged” Reeve to “study monetary proposals for curing unemployment”. Reeve made no reference to a unique Chicago monetary tradition.

vi Tavlas (chapter 27 [1979], 927) denied that he had only partially read Davis’ book: “So much for Mr. Davis’ empiricism”.

vii Hans Neisser (1934, 441-3), writing in the JPE, also described underconsumptionism as a non-monetary theory of crises. Neisser contrasted the “classical type of underconsumption theory [which] rejects from the outset all purely monetary considerations based on the quantity theory of money” with the “more primitive” approach of Foster and Catching in which the quantity of money increases in response to profit making transactions. Laidler (1999, 169, n16) commented that for Foster and Catching, the monetary system played a role in “generating underconsumptionism”.

viii Tavlas (chapter 29 [1981], 1137, n2) stated that “Humphrey [1971, 1973] never refers to Foster and Catchings”. In fact, Humphrey (chapter 17 [1973], 461) does, in passing, refer to Foster and Catching.

ix Aschheim and Tavlas (1996, 416, 409-10) described Laidler’s Golden Age of the Quantity Theory as “indispensable for future scholars of monetary thought”. They also disputed “Laidler’s attribution of the origination of the wage-stickiness hypothesis to Marshall and Pigou”, offering as examples Henry Thornton’s (1802) Paper Credit and John Gray who “articulated “one of the first monetary growth rules found in the literature and one that directly influenced the Chicago money-supply growth rate rule of the 1930s (see Tavlas 1977, [chapter 30 [1977]])”. However, in Golden Age of the Quantity Theory, Laidler (1991, 116, n30) stated that he did “not mean to suggest that [W.S.] Jevons originated the idea of money wage stickiness. It can be found, for example, in Thornton’s Paper Credit (1802) …”.

x Douglas and Aaron Director (1931) devote a little over 10% of The Problem of Unemployment to monetary factors.

xi After he retired from the Treasury, Hawtrey was Henry Price Research Professor at the Royal Institute of International Affairs, 1947-1952 (Davis 1981, 204).

xii For a similar conclusion, see Patinkin (1995, 361-2). See also Johnson (1975, 124) for critical perspective on the influence of ideology on Cambridge economics.

xiii The editors of the JPE formed a different judgement about Tavlas’ work than one of their nominated referees (such differences are, of course, the lifeblood of scholarly disputes).

xiv The last sentence of Laidler’s (chapter 39 [1999], 241) letter to the Journal of Economic Perspectives was edited without his knowledge or permission. The last sentence of his submitted letter reads: “A perusal of published work by, among others, Karl Brunner (1968), Thomas Humphrey (1971), Roger Sandilands (1990) Frank
Steindl (1996) and myself (Laidler 1993, 1998), all of which Tavlas has overlooked on this occasion, will reveal this in much more detail than can be set out in a letter”. This change may have exacerbated Tavlas’ suspicion that his work was being ignored.

xv For a discussion, see Leeson 2000.

xvi Laidler had been criticised a quarter of a century earlier by Joan Robinson (1973, ix) in her self-appointed role as one of Keynes’ “Bulldogs” (Samuelson 1994, 25). Laidler was a young award winning economist; but as President of Section F of the British Association for the Advancement of Science (BAAS) and editor of After Keynes Robinson (1973) marred the award ceremony by expressing contempt for Laidler, the 1972 Lister Lecturer, who she thought was a co-conspirator in the attempt to return economics to pre-Keynesian (i.e. quantity theory) perceptions (the Lister Lecturer was chosen by the BAAS committee, including Harry Johnson, not the President of Section F). According to Robinson (1972, 86-7) the quantity theory had been revived by “modern Chicagoans led by Milton Friedman … There is an unearthly, mystical element in Friedman’s thought”. Citing uncritically Patinkin (chapter 5 [1969]) Robinson continued: “In so far as [Friedman] offers an intelligible theory, it is made up of elements borrowed from Keynes”.

xvii Although the discovery of this memorandum pre-dates the Laidler-Tavlas exchange (see the brief references in Rees 1973, 37, and Sandilands 1990), its significance had not been adequately appreciated until Sandilands obtained a copy of the full manuscript from Princeton University's Manuscript Library in 2000.

xviii Watkins found an “obiter dicta” from The General Theory to indicate Keynes’ (1936, 205-6, 234) support for components of the proposal. In 1934, Paul Samuelson (1996, 148-9), a Chicago undergraduate, became converted to this proposal to eliminate factional reserve banking.

xix Albert Hart had been a graduate student with Friedman at Chicago (Phillips 1995, chapter 4; Friedman and Friedman 1998, 39-40). Hart’s essay was reprinted in Readings in Monetary Theory selected by a committee of the AEA, co-chaired by Lloyd Mints (Lutz and Mints 1952) and published just as Friedman began planning the Workshop in Money and Banking. It is safe to assume that Friedman was aware of Hart’s essay in the period that he was writing his ‘Restatement’ since in the early 1950s he prescribed the Readings to his students (Hammond 1999, 462). Shortly afterwards – as “a student of Henry Simons and Lloyd Mints” – Friedman (1960, 65-6) referenced the Hart essay and proposed to expand on the “original ‘Chicago Plan of Banking Reform’ in only one respect” by proposing that interest be paid on the 100% reserves.

xx Moreover, the “Chicago Plan” involved the objective of an increase in prices which does not immediately appear to be easily reconcilable with the orthodox quantity theory: “That the administration announce and pursue a policy of bringing about, by fiscal and monetary measures, an increase of fifteen (15) per cent in Wholesale Prices”. At the same time, “Adoption of the reserve guarantee arrangements, far from being inflationary, would actually involve, by comparison with conditions of the
recent past, a marked reduction in the quantity of circulating media” (cited by Phillips 1995, 196-7).

xxi The Plan was described in a Chicago Public Policy Pamphlet as having been “presented in a number of different forms, varying in detail” (Whittlesey 1935, 21; Gideonse 1935, iii).

xxii Soddy was unlikely to have created an anti-quantity theory oral tradition since his students, such as Kenneth Boulding, slept through his chemistry lectures (Daly 1980, 483, n4; see also Gaitskell 1933, 383).

xxiii Soddy (1934, 173, 131-2, 201; 1943, 25) opposed the “proposals of the Socialists” to nationalise banking on the grounds that it would not help to secure a stable price level. He outlined a 4% money growth rule which he attributed to Gustav Cassels and which he believed would preserve the value of money. He was also an early advocate of freely floating exchange rates as a vehicle to facilitate free trade a proposal that Friedman would later be associated with. Friedman (chapter 2 [1956], 16) objected to the “reaction against the quantity theory in the 1930s … The demand for money, it was asserted was a will-o’-the-wisp”. Referring to Fisher’s Purchasing Power of Money Soddy (1933a, xix-xxi) concluded that the velocity of circulation was “a will-of-the-wisp”.

xxiv Charles W. Eliot II became executive officer of the Board, Wesley Mitchell was also recruited as was Charles E. Merriam from Chicago’s Department of Politics who described the purpose of the Board as the creation of “a plan for national planning” (cited by Brinkley 2000, 174).

xxv Shortly afterwards, Chicago surpassed Philadelphia as the nation’s second largest city and won the right to host the World’s Fair celebrating the 400th anniversary of Columbus’ “discovery” of America. The Fair attracted millions of visitors and stimulated great interest in urban planning: “nowhere was this matter discussed more than in Chicago (Wrigley 1983, 58). Frederick Law Olmsted was recruited to recommend a site for the Fair. Two other architects involved in the project, Daniel Burnham and John Root, were associated with “the so-called Chicago School that paved the way to contemporary design” (Reps 1965, 498; Peterson 1996, 48). Simultaneously, John D. Rockefeller began his endowment of the University of Chicago (Turner 1984, 172). The “Chicago School of Sociology” was formed “in the two decades after the Plan of Chicago” (Fishman 2000a, 70; Knight 1924, 250; Ogburn 1934; Smith 1988). The Chicago School” of politics also acquired a “stunning impact … on the profession” (Simon 1991, 62). At a 1955 conference on ‘The State of the Social Sciences’ reference was made to the Chicago contributions to the social sciences made by John Dewey, J. Laurence Laughlin and James Angell’s father, the psychologist, James Roland Angell (Harris 1956, 1).

xxvi Such concerns were reflected in the JPE, and later republished in Landmarks in Political Economy (Hamilton, Rees, and Johnson 1962). One Chicago economist writing in the JPE referred to plans “for relieving the terminal difficulties at Chicago” which had been “advocated more or less urgently for twenty years” (Hill 1962 [1906], 64). Chicago was regarded as “typically a city of rugged individualism” (Wrigley
1983, 58). But nationalisation was the preferred solution: “It is hardly conceivable that the delay in adopting so great an improvement over the present method could have been worse under government ownership” (Hill 1962 [1906], 64).


xxviii President Theodore Roosevelt sought to initiate a “second national plan” to “control the mighty commercial forces” which American civilisation had unleashed. This “national plan” involved conservation, railways and city planning (Lacey 2000, 117). The motto of the City of Chicago is Urbs in Horto (“City set in a Garden”). In 1907, President Roosevelt described the Chicago parks as “one of the most notable civic achievements in any American City” (cited by Draper 1996, 100). Chicago was a pioneer in the search for the science of city planning” (Draper 1996, 104). The onset of the depression encouraged the parks to form an amalgamated Chicago Park district. This was achieved in 1934, which enabled the parks to qualify for significant WPA assistance.

xxix Wallace had been one of Fisher’s monetary reformers as the first Vice President of the Stable Money League (Fisher 1934a, 104; Schapsmeier and Schapsmeier 1968, 90-1; Markowitz 1973, 17-18). He was one of two disciples of Henry L. Moore (who retired from Columbia in 1929). The other disciple was Henry Schultz who persuaded Friedman to spend his second graduate year at Columbia (Friedman and Friedman 1998, 38-9; Stigler 1962, 17).

xxx Veblen had been recruited to Chicago by Laughlin (Friedman 1987).

xxxi In 1947, Tugwell was appointed chairman of Chicago’s graduate curriculum in planning (Scott 1969, 468).

xxxii This required textbook was Economic Analysis and Public Policy by Jean Bowman and a Chicago graduate George Bach (who had referred to the Chicago “oral tradition” in his doctoral dissertation). Buckley noted with alarm that this text was also prescribed at Chicago and 65 other universities. In a more advanced course, Buckley was obliged to read Simons’ Positive Program for Laissez Faire which outlined “a sure program for the destruction of the free economy”. By 1950-51, Simons’ essay had become required reading in Economics 10.